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Supreme Court, U.S.
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No. 97-334

In The

Supreme Court of the United States

October Term, 1996

CHARLES G. MILDEN and SUSAN P. MILDEN,

Petitioners,

vs.

JAMES J. JOSEPH, Chapter 7 Trustee,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

Despite the allegations of plaintiffs, the following are the actual questions, with regard to this real party in interest, Frank A. Barcott, an individual, dba, Frank A. Barcott Security and Investigation ("Barcott"), presented by this Petition:

1. Whether Petitioners may argue that the underlying bankruptcy was wrongfully converted to a Chapter 7 proceeding when they did not timely appeal from the conversion order?

2. Whether the bankruptcy and district courts had jurisdiction to approve the trustee's settlement of the estate's state court lawsuit?

LIST OF PARTIES

Charles G. Milden and Susan P. Milden, Petitioners, are Chapter 7 debtors.

James J. Joseph is the trustee of the Chapter 7 Milden Estate.

State of the Art, Inc. is a creditor of the Milden estate.

David S. Samuels, George Riviere and David W. Hanna are officers of State of the Art, Inc.

Robertson, Stephens & Co., is related to the State of the Art issues.

TA Associates is related to the State of the Art issues.

Frank A. Barcott, an individual, dba Frank A. Barcott Security and Investigations is one of the defendants in the state court action that was settled with the Chapter 7 Trustee in Bankruptcy.

Walter Dellinger, Solicitor General of the United States

United States of America, Office of the United States Trustee.

TABLE OF CONTENTS

	Page
Questions Presented	i
List of Parties	ii
Table of Contents	iii
Table of Citations	iv
Introduction	1
Reasons for Denying the Writ	2
I. The Bankruptcy And District Courts Properly Approved And Affirmed The Barcott Settlement.	2
A. Preemption Issue	3
B. Due Process Issue	4
C. Personal Injury Issue	4
II. "Personal Injury" Exemption Claim (Item 6 On P. 4 Of Petitioners' Petition).	6
III. Petitioners Did Not Timely Appeal The Chapter 7 Conversion Order And So Cannot Object To It Now (Item 1 On P. 4 Of The Petition).	6
Conclusion	7

Contents

Page

TABLE OF CITATIONS

Cases Cited:

Bronner v. Gill, 135 B.R. 645 (9th Cir. BAP 1992) ... 5

In re A & C Properties, 784 F.2d at 1381 4

In re Reberor, 89 B.R. 314 (N.D.N.Y. 1988) 6

In re Souza, 795 F.2d 855 (9th Cir. 1986) 7

People v. Kings Point Corp., 188 Cal. App. 3d 544 (1986) 3

Sierra Switchboard Co. v. Westinghouse Elec. Corp., 789 F.2d 705 (9th Cir. 1986) 5

United States v. Whiting Pools, Inc., 103 S. Ct. 2309, 462 U.S. 198 (1983) 5

Statutes Cited:

California Code of Civil Procedure § 704.140 6

11 U.S.C. § 541(a)(1) 3, 5

28 U.S.C. § 157 5

28 U.S.C. § 157(b)(1) 5

28 U.S.C. § 157(b)(5) 5

Contents

	Page
United States Constitution Cited:	
Article I	1
Article I, § 8	3
Article VI	3
Fifth Amendment	2, 4
Tenth Amendment	2, 3
Rules Cited:	
Fed. R. Bankr. Proc. 8001(a)	6
Fed. R. Bankr. Proc. 8002(a)	6

INTRODUCTION

Petitioners' purported grounds for hearing, when seen through the rhetoric, are merely disagreements with the Courts' rulings. Petitioners would have their cake and eat it too, *to wit*, enjoy the benefits of Chapter 7 bankruptcy, but not the downside of the loss of personal assets. The orders of the bankruptcy court, which have been upheld by the district court, and the Ninth Circuit court, are all soundly based on statutes enacted under Article I of the United States Constitution, as well as the facts and evidence before those courts.

The settled and dismissed lawsuit filed in the Superior Court for the State of California for the County of Orange was never a "personal injury" case. The Ninth Circuit specifically confirmed that it was a claim for emotional distress, and was the property of the bankruptcy estate. There was no claim by Petitioners in the state court action for physical injury, nor was there a claim that the settlement proceeds were necessary for the support of Petitioners. (Appendix to Petition, p. 11)

The state court action was commenced when State of the Art, Inc. ("SOTA") filed suit against Charles Milden almost seven years ago. The Mildens in turn sued SOTA, Barcott and two other defendants in March 1991. The two actions were consolidated. Four causes of action were alleged against Barcott: intentional and negligent infliction of emotional distress, negligence and defamation. Appellants' Excerpts of Record in Ninth Circuit appeal ("E.R.") at p. 194, n.1.

Seven months later, the Mildens filed Chapter 11 bankruptcy. In October 1992 the bankruptcy court granted the United States Trustee's motion to convert the case to a liquidation proceeding under Chapter 7. Appellees' Joint Supplemental Excerpts of Record in Ninth Circuit appeal ("S.E.R.") at Ex. 6. Petitioners did not timely appeal that order.

When trustee Ronald Clear was appointed to liquidate the bankruptcy estate, the state lawsuit became the property of the estate and Clear appeared and began litigating the case as the real party in interest. James J. Joseph was subsequently appointed successor trustee. By April 1993, Joseph and Clear settled with all of the defendants including Barcott. The January 1994 trial was taken off calendar and the superior court dismissed the case. Barcott has, since that time, been burdened with obsessive plaintiffs who will not let the case die.

REASONS FOR DENYING THE WRIT

I.

THE BANKRUPTCY AND DISTRICT COURTS PROPERLY APPROVED AND AFFIRMED THE BARCOTT SETTLEMENT.

Petitioners attack the Barcott settlement (item 2 on p. 4 of the Petition). The bankruptcy court approved each of the four defendants' settlements after several hearings. S.E.R. at Exs. 12 and 23. The district court affirmed these rulings on appeal and set forth its decisions in two comprehensive factual and legal analyses. E.R. at pp. 74-83 and 193-201.

Petitioners claim that the bankruptcy and district courts issued orders in excess of their jurisdiction. Petitioners base this claim on the following three incorrect legal contentions:

(1) Under the Tenth Amendment, state law preempts conflicting federal law with respect to state "property rights"

(2) The lower courts violated Petitioners' rights to due process by committing a Fifth Amendment taking of their property and,

(3) The lower courts wrongfully approved the settlements of a "personal injury" lawsuit.

Barcott will address each of these contentions in turn.

A. Preemption Issue

Petitioners contend that under the Tenth Amendment to the Constitution, state law must prevail over federal bankruptcy law with respect to "private property" in the form of state court lawsuits. However, their argument ignores the doctrine of preemption and must fail.

The Tenth Amendment provides that powers not otherwise delegated in the Constitution are reserved to the states or to the people. However, Article I, § 8 of the Constitution grants to Congress the power to establish uniform laws on the subject of bankruptcies. Article VI, the supremacy clause, makes federal laws the supreme law of the land. Thus Congress had clear authority to establish federal bankruptcy law which preempts conflicting state laws, if any.

Under both federal and state law, in a Chapter 7 liquidation proceeding, a debtor's lawsuits, state or federal, become property of the bankruptcy estate and are subject to a trustee's exclusive control. 11 U.S.C. § 541(a)(1) and *People v. Kings Point Corp.*, 188 Cal. App. 3d 544, 549 (1986). Thus state and federal law agree and do not conflict.

Under both federal and state law, California courts did not retain exclusive jurisdiction over the lawsuit but it became part of the estate upon Petitioners filing bankruptcy. *Id.* Further, even if there were a conflict in law, federal bankruptcy law would prevail in any event. For these reasons, Petitioners' Tenth Amendment argument lacks merit.

B. Due Process Issue

Petitioners' Fifth Amendment due process argument is that, by their orders, the lower courts deprived Petitioners of property. Specifically, they allege that they are entitled to retain the value of their estate in excess of that owed to their creditors and claim a taking occurred of the difference between what Petitioners believe their causes of action were worth and the amounts the trustee settled them for. However, as the district court correctly noted, the causes of action are estate property, not Petitioners, and so the challenged orders pertain to property that is not theirs.

The trustee's statutory duty is to liquidate the estate as quickly as possible for the benefit of creditors, not for the benefit of the debtors. The trustee had no duty to see to it that Petitioners have money left over once all the creditors are paid. As was found to be the case here, the trustee merely had to use reasonable judgment in settling the case within the range of reasonableness, considering pertinent factors such as the risk of litigation and the costs of ultimate recovery. *In re A & C Properties*, 784 F.2d at 1381. As such, Petitioners suffered no taking.

With respect to procedural due process, the record reflects that throughout the pendency of the underlying motions, orders and appeals, Petitioners have been indulged by the courts more than was warranted given their pro se status. Several hearings were held on the various issues. Clearly Petitioners were given notice and a chance to be heard at every turn. There is simply no evidence that Petitioners suffered any sort of due process violation.

C. Personal Injury Issue

Petitioners argue that the court erred in approving the settlement because the causes of action were for "personal

injury" and that a trial in district court was required under 28 U.S.C. § 157. This is incorrect both legally and under the facts of this case. E.R. at pp. 197-201.

All causes of action, whether for personal injury or not, are property of a bankruptcy estate by operation of law. 11 U.S.C. § 541(a)(1); *United States v. Whiting Pools, Inc.*, 103 S. Ct. 2309, 2313 n.9, 462 U.S. 198, 205 n.9 (1983); *Sierra Switchboard Co. v. Westinghouse Elec. Corp.*, 789 F.2d 705, 707 (9th Cir. 1986); and *Bronner v. Gill*, 135 B.R. 645, 647 (9th Cir. BAP 1992). They remain property of the estate, subject to the trustee's administration and control, unless they are abandoned or exempted, neither of which occurred in this case. Because the causes of action here are and always have been property of the estate, it was up to the trustee to settle or try the case and here he elected to settle.

Upon reaching each of the settlements of this case, the trustee properly sought and obtained bankruptcy court approval. The bankruptcy court in turn properly supervised the trustee's administration of this estate asset in hearing the trustee's motions for orders approving the various compromises (*i.e.*, settlements) as core proceedings within its statutory jurisdiction as provided in 28 U.S.C. § 157(b)(1). The hearings on the trustee's motions concerning the settlements were not "trials" of the case.

Thus, Petitioners' argument that under 28 U.S.C. § 157(b)(5) a trial in district court was required is untenable. The causes of action have been affirmatively found to involve no "personal injury" within the meaning of this statute and the trustee settled the case and so no trial was required.

II.

"PERSONAL INJURY" EXEMPTION CLAIM (ITEM 6 ON P. 4 OF PETITIONERS' PETITION).

Petitioners take issue with the bankruptcy court order sustaining the trustee's objections to the amended exemption claims made pursuant to California Code of Civil Procedure § 704.140. By that amended claim, Petitioners sought to exempt the Barcott and SOTA settlement proceeds and/or the causes of action alleged against them by claiming that their emotional distress and defamation causes of action were claims for personal injury. S.E.R. at Ex. 16. The bankruptcy court sustained the trustee's objections on this issue. S.E.R. at Ex. 21. The district court on appeal found no basis for disagreeing with the bankruptcy court's ruling that none of the Petitioners' claims involved bodily injury. S.E.R. at pp. 200-201.

III.

PETITIONERS DID NOT TIMELY APPEAL THE CHAPTER 7 CONVERSION ORDER AND SO CANNOT OBJECT TO IT NOW (ITEM 1 ON P. 4 OF THE PETITION).

The bankruptcy court granted the United States Trustee's motion to convert the case to a Chapter 7 proceeding and entered its order to that effect in October 1992. S.E.R. at Ex. 6. A Chapter 7 conversion order is final for the purposes of appeal because it substantially affects the debtor's property rights. *In re Reberor*, 89 B.R. 314, 321 (N.D.N.Y. 1988). With this, Petitioners agreed in their opening brief to the Ninth Circuit (p. 21). No notice of appeal concerning the conversion order was ever filed.

Under Fed. R. Bankr. Proc. 8001(a) and 8002(a) Petitioners

had ten days from the entry of the conversion order to file a notice of appeal. They did not do so. Petitioners are not entitled to this type of relief because the requirement that a timely notice of appeal be filed is jurisdictional. *In re Souza*, 795 F.2d 855, 857 (9th Cir. 1986). As such, all sections of the petition which address or relate to the Chapter 7 conversion of the bankruptcy estate must be disregarded as irrelevant.

CONCLUSION

Based on the foregoing, the bankruptcy, district court, and Ninth Circuit rulings concerning the Barcott settlement and the sustaining of the trustee's objections to the Petitioners' personal injury exemption claims were proper. There is no showing of abuse of discretion or misapplication of the law. Rather, the lower courts rendered comprehensive and accurate assessments of this case and proper legal rulings after consideration of all pertinent evidence before them. The petition should be denied.

Respectfully submitted,

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